

**STATE OF WASHINGTON  
OFFICE OF THE INSURANCE  
COMMISSIONER**



**FINANCIAL EXAMINATION  
OF  
US BRANCH OF INDUSTRIAL - ALLIANCE PACIFIC  
LIFE INSURANCE COMPANY  
VANCOUVER, CANADA  
NAIC CODE #84514  
DECEMBER 31, 2002**

Participating States:  
Washington

Order No. G 02-07  
US Branch of Industrial-Alliance  
Pacific Life Insurance Company  
Exhibit A

RECEIVED  
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INSURANCE COMMISSIONER  
COMPANY SUPERVISION

CHIEF EXAMINER AFFIDAVIT

I hereby certify I have read the attached Report of the Financial Examination of the US Branch of Industrial-Alliance Pacific Life Insurance Company of Vancouver, British Columbia, Canada. This report shows the financial condition and related corporate matters as of December 31, 2002.



Patrick H. McNaughton  
Chief Examiner

3-4.05

Date

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SALUTATION

Seattle, Washington  
March 4, 2005

The Honorable Kevin McCarty  
Director of Insurance Regulation  
Chairman, NAIC Financial Condition (E) Committee  
Florida Department of Financial Services  
The Larson Building  
200 E. Gaines Street, Room 101  
Tallahassee, Florida 32399-0301

The Honorable John Morrison  
Commissioner  
NAIC Secretary Western Zone  
Montana Department of Insurance  
840 Helena Avenue  
Helena, MT 59601

The Honorable Mike Kreidler  
Washington State Office of the Insurance Commissioner (OIC)  
Insurance 5000 Building  
5000 Capital Blvd.  
Tumwater, WA 98504-0255

Dear Commissioners:

In accordance with your instructions and in compliance with the statutory requirements of RCW 48.03.010, an association examination was made of the corporate affairs and financial records of

US BRANCH OF INDUSTRIAL - ALLIANCE PACIFIC LIFE INSURANCE  
COMPANY

of  
Vancouver, British Columbia, Canada

hereinafter referred to as "IAP-US" or "the Company", at its home office located at 2165 Broadway W., Vancouver, British Columbia, Canada. The following report on the examination is respectfully submitted showing the condition of the Company as of December 31, 2002.

## **SCOPE OF EXAMINATION**

This examination covers the period January 1, 1998 through December 31, 2002 and comprises a comprehensive review of the books and records of the Company. The examination followed the statutory requirements contained in the Washington Administration Code (WAC), and Revised Code of Washington (RCW), and the guidelines recommended by the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook (FCEH). The examination included identification and disposition of material transactions and events occurring subsequent to the date of examination that were noted during the examination. The findings of the previous examination report were reviewed and any items that were not satisfactorily addressed by the Company are discussed later in the report.

Corporate records, external reference materials, and various aspects of the Company's operating procedures and financial records were reviewed and tested during the course of this examination and are commented upon in the following sections of this report. In addition, the Company's certified public accountant's (CPA's) work papers were reviewed and utilized, where possible, to facilitate efficiency in the examination.

## **INSTRUCTIONS**

The examiners reviewed the Company's filed 2002 NAIC Annual Statement as part of the statutory examination. This review was performed to determine if the Company completed the NAIC Annual Statement in accordance with the NAIC Annual Statement Instructions and to determine if the Company's accounts and records were prepared and maintained in accordance with Title 48 RCW and Title 284 WAC, and the NAIC Statements of Statutory Accounting Principles (SSAP) as contained in the Accounting Practices and Procedures Manual (AP&P).

The following summarizes the exceptions noted while performing this review.

### **1. Audited Financial Statements**

IAP - US does not file audited financial statements with the OIC. The external audit is performed on Industrial Alliance Pacific Life Insurance Company (IAPL) financial statements (U.S. branch and Canadian branch), which are then filed with the OIC on the basis of Canadian Generally Accepted Accounting Principles (GAAP) and in Canadian dollars. According to RCW 48.05.073, every insurer shall file its financial statements in accordance with the AP&P which includes the NAIC Annual Statement Instructions. According to the NAIC Annual Statement Instructions, Annual Audited Financial Reports section, page 44, #14 and the Annual Statement - General section, page 28, #13, the annual audited financial report for Canadian companies shall be the annual statement of total business on the form filed with their domiciliary supervision authority, audited by an

independent chartered accountant, presented in U.S. dollars, and attested to by the independent chartered accountants.

WAC 284-07-100(1) requires... "an annual examination by independent certified public accountants of the financial statements reporting the financial position and results of operations of insurers." The Company filed IAPL Canadian dollar audited financial statements, on a Canadian GAAP basis, with the Office of the Superintendent of Financial Institutions and the OIC. But those statements were different from the U.S. dollar financials which appeared in the IAP-US NAIC Annual Statement filed with the OIC.

WAC 284-07-130(1) states that "The annual audited financial report shall report the financial position of the insurer as of the end of the most recent calendar year and the result of its operations...for the year then ended in conformity with statutory accounting practices prescribed, or otherwise permitted, by the commissioner."

**In accordance with WAC 284-07-130 (1) and (2)(f); WAC 284-07-100 (1); and the AP&P, IAP-US is instructed to attach to the audited IAPL financial statements a supplemental schedule which represents in U.S. dollars the financial position and results of operations of IAP-US as they were presented in the NAIC Annual Statement filed with the OIC, accompanied by appropriate notes to reconcile between the financial statements filed in Washington and those filed with the Canadian regulators.**

## **2. Custodial Agreement**

The Company's custodial agreement does not contain some provisions required by the FCEH. However, although the Company's response to General Interrogatory # 22 says that the agreement does comply with the FCEH, it does not contain the following FCEH required provisions:

- 1) The agreement with agents ("subcustodians") shall state that, "... the agents shall be subjected to the same liability for loss of securities as the custodian".
- 2) "That if the custodial agreement has been terminated or if 100% of the account assets of any one custody account have been withdrawn, the custodian shall provide written notification, within three business days of termination or withdrawal, to the insurer's domiciliary commissioner".
- 3) "The custodian and its agents, upon reasonable request, shall be required to send all reports which they receive from a clearing corporation or the Federal Reserve book-entry system which the clearing corporation or the Federal Reserve permits to be redistributed and reports prepared by the custodian's outside auditors, to the insurance company on its respective systems of internal control".

4) "That the custodian shall secure and maintain insurance protection in an adequate amount".

5) "That the foreign bank acting as a custodian, or a U.S. custodian's foreign agent, or a foreign clearing corporation is only holding foreign securities or securities required by the foreign country in order for the insurer to do business in that country. A U.S. custodian must hold all other securities".

In addition, since the Company stated in General Interrogatory #22 that the Custodial Agreement complies with the FCEH provisions, it did not comply with RCW 48.05.250 (1) which requires the Company to file a true condition of its financial transactions, condition and affairs.

**The Company is required to follow the NAIC's Annual Statement requirements as noted in WAC 284-07-050(2). Adherence to the 2002 FCEH is one of those requirements. The Company is instructed to correct all of the deficiencies noted above and execute a revised or amended custodial agreement.**

### **3. Conflict of Interest**

The following deficiencies were noted in the conflict of interest disclosure forms:

1. Required disclosures were occasionally left blank.
2. Forms were occasionally undated, unsigned or both.
3. For several years under examination, disclosure forms could not be located for some of the officers and directors listed on the jurat page of the NAIC Annual Statement.

**RCW 48.05.370 states, "Officers and directors of an insurer... shall be deemed to stand in a fiduciary relation to the insurer, and shall discharge the duties of its respective positions in good faith, and with that diligence, care and skill which ordinary prudent men would exercise under similar circumstances in like positions." In order to monitor compliance with this statute, the Company is instructed to obtain and review conflict of interest declarations from all employees, as required by the conflict of interest section of its Code of Conduct.**

### **4. NAIC Annual Statement Preparation**

According to RCW 48.05.073, every insurer shall file its financial statements in accordance with the AP&P. In preparing its NAIC Annual Statement, IAP – US did not follow the NAIC Annual Statement instructions in the following areas:

- **Deposit Liabilities** – Annuities which did not subject the reporting entity to any risks arising from policyholder mortality or morbidity were recorded as premiums and reserves were established. Per SSAP #52, such contracts should not be

accounted for as insurance contracts and amounts received should not be reported as revenues but rather recorded directly to the deposit liability account.

- **Federal Income Tax Recoverable** – The Company did not calculate the correct amount of deferred tax asset to be admitted on the Annual Statement. An examination adjustment, A1, of \$4,046,257 was made to correct the allowable deferred taxes.
- **Amounts Held for Agents** – This line item, page 3, line 18 included general ledger accounts that should have been included on page 3, line 10 – Commissions to Agents Due or Accrued.
- **Capital Gains** – Contrary to the NAIC Annual Statement instructions, the Company did not report on “The Exhibit of Capital Gains (Losses)” the capital gains (losses) used in the calculation of the Interest Maintenance Reserve (IMR).
- **Schedule D** – The Company did not include any indication that certain securities were provisionally exempt. There were also some securities that were reported with the incorrect NAIC designation.
- **Rental Income** – The Company did not correctly account for rental income on foreclosed property nor did it depreciate the property. The amounts did not have a material effect on the financial statements.

The above deviations from the AP&P were corrected on the 2003 NAIC Annual Statement. The following errors were not corrected on the 2003 NAIC Annual Statement:

- **Cash** – A Certificate of Deposit held as a security by New Mexico which should have been properly reported on Schedule E, part 2, was instead included on Schedule DA.
- **Pension Plans** – The Company did not disclose or describe in the Notes to Financial Statements that the employees who perform work for the U.S. Branch are covered under pension plans maintained by the parent.
- **General Interrogatories** - The Company reported an amount for common and preferred stock on item number 17 on the NAIC Annual Statement. Since this is a branch operation, the Company does not report any stock on page 3, lines 29 and 30 and should not report any amount for this item in the General Interrogatories.
- **Catastrophic Reinsurance** – The Company did not report its catastrophic reinsurance treaty with Aon Re Canada on Schedule S.
- **Current Federal Income Tax Accrual** – The Company netted its current federal income tax payable and receivable and reported it as a liability on the NAIC Annual Statement instead of reporting the receivable as an asset and the payable as a liability.
- **Policy Loan/Cash Value** – The Company used the policy value when testing loan balances to ensure that the amount of policy loan does not exceed the cash value of the policy per SSAP No. 49, paragraph 5, but the policy value does not take into consideration surrender values or the policy reserves established, so the Company may make policy loans that are greater than their cash value.



- **Acquisition Date of Bonds** – When bonds were acquired, the Company recorded them on the settlement date instead of the trade date as required by SSAP No. 26, paragraph 4.
- **Impaired Bond** – The Company reported a permanently impaired bond as part of its IMR instead of its Asset Valuation Reserve (AVR). A examination adjustment, A2, was made for \$814,123 to correct this mis-reporting.

**The Company is instructed to comply with RCW 48.05.250 and file a true statement of its financial conditions, transactions and affairs; with RCW 48.05.073 which requires the filing of its financial statements in accordance with AP&P; and WAC 284-07-050(2) which requires adherence to the NAIC Annual Statement Instructions and AP&P.**

### **COMMENTS AND RECOMMENDATIONS**

#### **1. Suspense Accounts**

The Company does not clear its suspense accounts in a timely manner. Three of the suspense accounts reviewed contained items dating from 1999. The dollar amounts are small, but it is good business practice to clear such accounts in a timely manner. The Company also does not have any written procedure for the timely clearing of suspense accounts.

**It is recommended that the Company institute and enforce a written policy requiring that suspense accounts be cleared within a reasonable time frame.**

#### **2. Cash Control**

The Company does not maintain a record of checks received in the mailroom. The checks are sent to the appropriate departments without being restrictively endorsed or recorded in any way.

**To decrease the likelihood of misappropriation while increasing the control over negotiable instruments, the Company should institute procedures to ensure that such funds are recorded and restrictively endorsed upon receipt.**

#### **3. Journal Entry Approval**

A review of the Company's monthly journal entries revealed that some are not approved by an authorized party.

**Control is a very important part of the accounting process. By not indicating that approval has taken place, the Company is leaving itself open to errors that may or may not be discovered during the reconciliation process. In order to maintain and**

**record control over the processing of journal entries, it is recommended that all journal entries be approved and signed by a competent authority.**

#### **4. Reinsurance Analysis**

The Company does not perform an evaluation of reinsurance to determine if any changes should be made to the contracts or if the reinsurance is cost-effective.

**To ensure that its reinsurance contracts are reasonably priced, it is recommended that the Company evaluate them at least annually. This would include evaluating recoveries and coverage against historical and anticipated loss ratios.**

#### **5. Schedule D Preparation**

The Company's preparation of Schedule D (Schedule of Long Term Bonds and Stocks) is time consuming and error prone. The Company pieced numbers together from various sources for the schedule, resulting in errors. Some insurance companies require the investment management company to prepare Schedule D as part of its services.

**It is recommended that the Company work with its external investment manager to at least obtain more assistance in preparing its Schedule D.**

### **COMPANY PROFILE**

#### **Company History**

The prior examination was performed as of December 31, 1997, and covered the period January 1, 1993 to December 31, 1997.

On April 29, 1967, Industrial –Alliance Pacific Life Insurance Company (IAPL) was incorporated under Canadian law in the name of The North West Life Assurance Company of Canada and commenced business on June 22, 1967. In 1971, The Company was granted a Certificate of Authority for the Company to use Washington State as a state of entry to transact insurance in the United States, pursuant to RCW 48.35.010, thus creating a U.S. branch. In 1973, the Company commenced business as an alien insurer.

On July 8, 1982, The North West Life Assurance Company of Canada was purchased by Industrial Alliance Life Management Corporation, which was ultimately controlled by Industrial-Alliance Life Insurance Company of Quebec, Canada (IAL).

In September of 2000, The North West Life Assurance Company of Canada changed its name to Industrial – Alliance Pacific Life Insurance Company.

## **Territory and Plan of Operation**

The Company markets universal life, whole life, term and single premium immediate and deferred annuity contracts in 22 states. The majority of the Company's business is generated in California, Washington, and Texas.

The Company directly appoints and compensates agents and brokers to sell its products.

## **Growth of Company**

The Company's growth, as reported in its filed NAIC Annual Statements, is illustrated below.

	<u><b>Assets</b></u>	<u><b>Liabilities</b></u>	<u><b>Capital and Surplus</b></u>
<b>1998</b>	\$257,371,781	\$225,875,501	\$31,496,280
<b>1999</b>	255,919,672	221,666,490	34,253,182
<b>2000</b>	247,137,054	209,513,670	37,623,384
<b>2001</b>	256,106,132	213,996,095	42,110,037
<b>2002</b>	258,228,453	226,611,187	31,617,266

	<u><b>Premiums</b></u>	<u><b>Net Investment Income</b></u>	<u><b>Annuity Benefits</b></u>
<b>1998</b>	\$16,171,684	\$18,704,499	\$22,785,465
<b>1999</b>	15,222,769	17,761,698	20,024,931
<b>2000</b>	22,926,965	17,194,855	22,548,615
<b>2001</b>	20,833,615	16,871,158	12,863,497
<b>2002</b>	26,319,832	15,572,880	13,643,326

## **Business in Force By State**

Alabama	\$457,283	Montana	2,031,975
Alaska	1,511,160	Nebraska	506,514
Arizona	67,701,596	Nevada	22,861,956
Arkansas	637,772	New Hampshire	527,752
California	1,215,533,913	New Jersey	1,022,380
Colorado	37,203,666	New Mexico	5,554,878
Connecticut	761,361	New York	3,160,701
Delaware	40,000	North Carolina	1,469,105
District of Columbia	70,000	Ohio	1,532,336
Florida	8,509,879	Oklahoma	3,518,129
Georgia	2,173,252	Oregon	11,382,206
Hawaii	17,866,367	Pennsylvania	740,532

Idaho	31,816,276	South Carolina	130,268
Illinois	\$2,716,184	South Dakota	270,000
Indiana	1,379,410	Tennessee	1,027,264
Iowa	597,818	Texas	118,802,879
Kansas	912,850	Utah	7,703,469
Kentucky	311,288	Vermont	100,000
Louisiana	490,710	Virginia	2,427,785
Maine	185,455	Washington	71,934,911
Maryland	622,094	West Virginia	60,243
Massachusetts	614,825	Wisconsin	1,198,532
Michigan	1,182,355	Wyoming	417,000
Minnesota	2,154,475	Guam	25,202
Mississippi	115,000	Puerto Rico	11,066
Missouri	654,713	Canada	4,683,157

Total Business in Force by State \$1,659,319,942

### **Affiliated Companies**

Industrial Alliance Life Insurance Company 99.9% Ownership

There are twenty other affiliates of IAPL, most of whom are 100% owned by IAL.

### **Intercompany Contract**

As of December 31, 2002, the Company was a party to the IAL Intercompany General Services Agreement which was effective January 1, 2001.

## **MANAGEMENT AND CONTROL**

### **Board of Directors**

As of December 31, 2002, the Company was controlled by an eleven-member Board of Directors (BOD).

<b>Name</b>	<b>Principal Business Affiliation</b>
Yvon Charest	President and Chief Executive Officer, Industrial-Alliance Life Insurance Company
Yvon Cote	Vice President and General Manager, Finance & Investments, Industrial Alliance Life Insurance Company
Raymond Garneau	Chairman of the Board -- Industrial - Alliance Life Insurance Company
John Baldev Gill	President and Treasurer, Industrial Alliance Pacific Life Insurance

Rom Johnson Markin	Company Maughmer Freedom Philosophy Chair and Professor, Washington State University
Gerald Allan Bell McGavin	President, McGavin Properties Ltd
Dale George Parker	Corporate Director
Normand Pepin	Executive Vice President, Industrial - Alliance Life Insurance Company
Blaize Horner Reich	Associate Dean, Executive Programs, Simon Fraser University
Henri Alfred Roy	Advisor to the Chairman, Telesystem Ltd
Warren Van Genderen	Partner, Meridian Capital, LLC

The Corporate Bylaws provide that the number of directors may be changed from time to time by amendment or by resolution of the BOD.

### **Officers**

The officers on December 31, 2002 were:

Raymond Garneau	Chairman
Yvon Charest	Vice Chairman & CEO
John Baldev Gill	President & Treasurer
Douglas Alexander Carrothers	Corporate Secretary

### **Committees**

The Board has an active Investment Committee, Audit Committee, Conduct Review Committee, Executive Committee, Human Resource Committee and a Pension Committee for the Defined Contribution Pension Plan.

### **Conflict of Interest**

The Company has two conflict of interest policies in place: one for directors, which was originally adopted in 1996, and one for officers and key employees, which was adopted in 1999. Upon appointment, the Directors are required to sign a disclosure statement. The statement is then examined for completeness, reviewed by the Audit Committee for resolution of potential conflicts, and put on file with the Human Resources Department. The Directors are responsible for reporting any subsequent potential disclosure items. Officers and key employees are annually required to sign a disclosure form, which is reviewed and filed with the Corporate Secretary. Any significant items are resolved in coordination with the legal department. The Company also has a Code of Business Conduct which was reviewed and adopted in 1996 for officers and in 1999 for other employees.

### **Fidelity Bond and Other Insurance**

The Company is a named insured on a fidelity insurance policy purchased by its parent. Coverage limits to \$10,000,000 are provided for all of the insured affiliates. For IAPL, the minimum amount recommended by the NAIC is \$800,000. The aggregate amount of coverage meets the minimum requirements.

IAP-US is also a named insured on property and liability insurance obtained by the parent. On December 31, 2002, the policies provided coverages for real and personal property, commercial general liability, umbrella/excess liability, financial institution fidelity bond, fiduciary liability, directors' and officers' liability, errors and omissions liability and managed care organization liability.

### **Officers', Employees', and Agents' Welfare and Pension Plans**

Company employees are covered under the IAPL Defined Contribution and Defined Benefit program.

Employees residing in the U.S. are offered a Simple IRA.

There are three different plans for Employees residing in Canada:

**Defined Contribution Plan** – for employees whose pay is based on sales bonuses/commissions, or a combination of sales bonuses/commissions and salary.

**Defined Benefit Plan** – for salaried employees with a mandatory participation stipulation for full time employees.

**Voluntary RRSP (Registered Retirement Savings Plan)** - Contributions are made solely by the employees. This voluntary plan is only available for Canadian residents.

## **CORPORATE RECORDS**

The Articles of Incorporation were amended since the previous examination date. On August 4, 2000, the name of The North West Life Assurance Company of Canada was changed to its current name, Industrial-Alliance Pacific Life Insurance Company.

The Bylaws were also amended since the previous examination date. On November 16, 1998, the BOD authorized issuance of an unlimited number of common or preferred shares, which was in compliance with Canadian statute and custom.

The shareholders meet annually. The Bylaws do not require the BOD to meet on a regular basis. The statute under which the Company is incorporated requires that the directors meet at least four times per year.

## **MORTALITY AND LOSS**

IAP-US provided copies of its actuarial workpapers and reserve reports as of December 31, 2002. Tests were performed on the underlying data, methods, and calculations as deemed necessary. Valuation reports and procedures were tested to establish that accurate and complete in-force information as of December 31, 2002 was represented in the valuation reports and workpapers. A sampling of contracts and payments was taken from active life and disabled life reserve reports, premium collection records and paid claims reports. The samples were tested for completeness and accuracy and it was determined that the Company's calculations were based on accurate and complete demographic data.

During the course of the examination, the actuary performed such testing of the Company's reserving methodologies and philosophies as was deemed necessary to form an opinion with respect to the items reported. The actuary relied upon the Company's listings and summaries of in-force policies and contracts.

The general examination emphasis was to review the methods, assumptions or other bases used to determine the reported NAIC Annual Statement items, and to determine whether the reported amounts are sufficient and in compliance with Washington law.

In the OIC Actuary's opinion, the methods, assumptions and methodologies used by the Company are generally appropriate, and all material relevant assets and liabilities on the NAIC Annual Statement were reported in accordance with accepted methods and principles.

## **REINSURANCE**

The Company assumes no reinsurance. It has a number of ceded reinsurance contracts covering various aspects of its operations. Most cessions are computed on a yearly renewable term basis and are with authorized reinsurers. One exception is an aggregate excess of loss treaty with a number of companies, some of which are unauthorized, but all of which are major reinsurers.

All the contracts have at least the minimum standard wording generally utilized to contain the Company's risk.

## **STATUTORY DEPOSITS**

The Company has the following Statutory Deposits:

<b><u>State</u></b>	<b><u>Type</u></b>	<b><u>Par Value</u></b>	<b><u>Market Value</u></b>	<b><u>Statement Value</u></b>
California	B	\$5,500,000	\$5,809,020	\$5,439,284
Washington	B	2,500,000	2,769,210	2,423,525
New Mexico	B	125,000	122,208	122,733

Florida

B

300,000 337,584

288,306

### **ACCOUNTING RECORDS AND INFORMATIONS SYSTEMS**

The management of IAP-US is sufficiently knowledgeable of information system processes. Systems development, acquisition and maintenance controls were evaluated to gain assurance that appropriate controls are in place for a company the size of IAP-US.

Operations and application controls were reviewed to determine the type of hardware installed, operating systems and proprietary software in use, back up and recovery facilities employed, and the controls exercised to maintain data security.

As required by NAIC FCEH guidelines, IAP-US has a formal, written disaster recovery plan and a business contingency plan that address the continuation of all significant business activities, including financial functions, telecommunication services and data processing services, in the event of a disruption of normal business activities.

### **SUBSEQUENT EVENTS**

None

### **FOLLOW UP ON PREVIOUS EXAMINATION FINDINGS**

All previous report instructions and comments were corrected.

### **FINANCIAL STATEMENTS**

Assets, Liabilities, Surplus and Other Funds

Summary of Operations

Reconciliation of Surplus For the Period Since the Last Examination

Analysis of Changes in Financial Statements As a Result of the Examination



**US BRANCH OF INDUSTRIAL - ALLIANCE PACIFIC  
LIFE INSURANCE COMPANY  
ASSETS, LIABILITIES, SURPLUS AND OTHER FUNDS  
DECEMBER 31, 2002**

	<u>BALANCE PER</u> <u>COMPANY</u>	<u>REF</u>	<u>EXAM</u> <u>ADJ</u>	<u>BALANCE PER</u> <u>EXAM</u>
<b><u>ASSETS</u></b>				
Bonds	\$84,887,880			\$84,887,880
Mortgage Loans - First Liens	128,563,721			128,563,721
Cash and short term investments	18,337,970			18,337,970
Real Estate - held for sale	669,622			669,622
Policy loans	16,945,237			16,945,237
Subtotal, cash and invested assets	<u>\$249,404,430</u>		<u>\$0</u>	<u>\$249,404,430</u>
Federal and foreign tax recoverable (Note #A1)	5,233,127	A1	(4,046,257)	1,186,870
Life insurance premiums and annuity considerations, deferred and uncollected	1,817,768			1,817,768
Investment income due and accrued	<u>1,773,128</u>			<u>1,773,128</u>
<b>TOTAL ASSETS</b>	<u><u>\$258,228,453</u></u>		<u><u>(\$4,046,257)</u></u>	<u><u>\$254,182,196</u></u>
<b><u>LIABILITIES</u></b>				
Aggregate reserve for life policies and contracts	\$215,601,266			215,601,266
Contract claims - life	1,373,178			1,373,178
Premiums and annuity considerations received in advance	96,902			96,902
Surrender values on cancelled policies	21,812			21,812
Interest Maintenance Reserve	130,056		687,934	817,990
General expenses due or accrued	(22,936)			(22,936)
Taxes, licenses and fees due or accrued excluding fit	37,590			37,590
Federal and foreign income taxes	1,517,733			1,517,733
Amounts withheld or retained by company as agent	17,106			17,106
Amounts held for agents account	594,496			594,496
Remittances and items not allocated	1,618,090			1,618,090
Dividends to stockholders declared and unpaid	2,252,643			2,252,643
Asset valuation reserve	1,991,362		(245,949)	1,745,413
Payable to parent	932,538			932,538
Aggregate write-ins for liabilities	<u>449,351</u>			<u>449,351</u>
<b>TOTAL LIABILITIES</b>	<u><u>\$226,611,187</u></u>		<u><u>\$441,985</u></u>	<u><u>\$227,053,172</u></u>
<b><u>SURPLUS AND OTHER FUNDS</u></b>				
Common capital stock	0			0
Reserve for Aids	600,000			600,000
Unassigned Funds (Note #A1)	<u>31,017,266</u>	A1&2	<u>(4,488,242)</u>	<u>26,529,024</u>
Capital and surplus	<u>31,617,266</u>		<u>(4,488,242)</u>	<u>27,129,024</u>
<b>TOTAL LIABILITIES, SURPLUS AND OTHER FUNDS</b>	<u><u>\$258,228,453</u></u>		<u><u>(\$4,046,257)</u></u>	<u><u>\$254,182,196</u></u>

**US BRANCH OF INDUSTRIAL - ALLIANCE PACIFIC  
LIFE INSURANCE COMPANY  
SUMMARY OF OPERATIONS  
YEAR ENDED  
DECEMBER 31, 2002**

	<u>BALANCE PER COMPANY</u>	<u>REF</u>	<u>EXAM ADJ</u>	<u>BALANCE PER EXAMINATION</u>
<b><u>INCOME</u></b>				
Premiums and annuity considerations	\$26,319,832			\$26,319,832
Net investment income	15,572,880			15,572,880
Commission and Expense Allowance	25,025			25,025
Amortization of Interest Maintenance Reserve (Note #A2)	158,857	A2	126,189	285,046
Aggregate write-ins for miscellaneous income	223,589			223,589
<b>TOTAL INCOME</b>	<b>\$42,300,183</b>		<b>\$126,189</b>	<b>\$42,426,372</b>
<b><u>BENEFITS</u></b>				
Death Benefits	\$3,109,977			\$3,109,977
Annuity Benefits	13,643,326			13,643,326
Surrender Benefits	2,819,232			2,819,232
Interest and adjustments on contracts	2,557			2,557
Increase in aggregate reserves for life and health policies and contracts	9,620,886			9,620,886
<b>TOTAL BENEFITS</b>	<b>\$29,195,978</b>		<b>\$0</b>	<b>\$29,195,978</b>
<b><u>EXPENSES</u></b>				
Commissions on premiums and annuity considerations	5,498,031			5,498,031
General insurance expenses	3,997,134			3,997,134
Insurance taxes, licenses and fees, excl. federal income tax	318,775			318,775
Increase in loading	314,538			314,538
Aggregate write-ins for expenses	58,661			58,661
<b>TOTAL EXPENSES AND BENEFITS</b>	<b>\$39,383,117</b>		<b>\$0</b>	<b>\$39,383,117</b>
Net gain from operations before dividends to policyholders and income taxes (Note #A2)	2,917,066	A2	126,189	3,043,255
Less Federal income taxes incurred (excl. tax on capital gains)	1,077,197			1,077,197
Net gain from operations after dividends to policyholders and income taxes but before realized capital gains (losses) (Note #A2)	1,839,869	A2	126,189	1,966,058
Net realized capital gains or (losses) less capital gains tax (Note #A2)	12,157	A2	(814,123)	(801,966)
<b>NET INCOME</b>	<b>\$1,852,026</b>		<b>(\$687,934)</b>	<b>\$1,164,092</b>

**US BRANCH OF INDUSTRIAL - ALLIANCE PACIFIC  
LIFE INSURANCE COMPANY  
SUMMARY OF OPERATIONS (CONTINUED)  
YEAR ENDED DECEMBER 31, 2002**

	BALANCE PER COMPANY	REF	EXAM ADJ	BALANCE PER EXAMINATION
<b>Capital and Surplus Account</b>				
Capital and Surplus, December 31, Previous Year	\$42,110,039			\$42,110,039
Net income (Note #A2)	1,852,026	A2	(687,934)	1,164,092
Change in net deferred income tax	167,632			167,632
Change in non-admitted assets and related items (Note #A1)	(660,319)	A1	(4,046,257)	(4,706,576)
Change in asset valuation reserve (Note #A2)	32,112	A2	245,949	278,061
Dividends to Sockholders	(2,252,643)			(2,252,643)
Aggregate write-ins	(9,631,581)			(9,631,581)
Net change in capital and surplus for the year	(10,492,773)		(4,488,242)	(14,981,015)
Capital and Surplus, December 31, 2002	<u>\$31,617,266</u>		<u>(\$4,488,242)</u>	<u>\$27,129,024</u>

**US BRANCH OF INDUSTRIAL - ALLIANCE PACIFIC  
LIFE INSURANCE COMPANY  
RECONCILIATION OF SURPLUS  
FOR THE PERIOD SINCE THE LAST EXAMINATION**

	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>
Capital and Surplus, December 31, Previous Year	\$42,110,039	\$37,623,384	\$34,253,182	\$31,496,280	\$29,313,745
Net income	1,852,026	3,268,246	4,210,831	2,047,212	2,299,642
Change in net unrealized capital gains (losses)				(70,000)	(352,791)
Change in unrealized foreign exchange capital gain		(54,030)			
Change in net deferred income tax	167,632	(289,950)			
Change in reserve on acct of change in valuation basis					
Change in non-admitted assets and related item	(660,319)	(154,800)	10,218	1,166,781	94,204
Change in asset valuation reserve	32,112	(7,677)	(311,807)	(390,119)	273,636
Amount of Currency Translation			(539,040)	9,776	(162,221)
Cumulative effect of changes in accounting principles		5,410,091			
Other		(685,225)		(6,748)	30,065
Dividends to Stockholders	(2,252,643)	(3,000,000)			
Interbranch Transfers	(9,631,581)				
Net change in capital and surplus for the year	(10,492,773)	4,486,655	3,370,202	2,756,902	2,182,535
Capital and surplus on December 31, 2002	<u>\$31,617,266</u>	<u>\$42,110,039</u>	<u>\$37,623,384</u>	<u>\$34,253,182</u>	<u>\$31,496,280</u>

**US BRANCH INDUSTRIAL - ALLIANCE PACIFIC**  
**Analysis of Changes in Financial Statements Resulting from the Examination**  
**As of December 31, 2002**

	<u>PER COMPANY</u>	<u>PER EXAMINATION</u>	<u>EXAMINATION ADJUSTMENT REFERENCE</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>	<u>TOTALS</u>
<b>Capital and Surplus, December 31, 2002 - Per Annual Statement</b>					<b>\$ 31,617,266</b>
<b><u>ASSETS</u></b>					
Federal Income Tax Recoverable	5,233,127	1,186,870	A1	(4,046,257)	
<b><u>LIABILITIES</u></b>					
IMR	130,056	817,990	A2	(687,934)	
AVR	1,991,362	1,745,412	A2	245,949	
Change in surplus					<u>(4,488,242)</u>
<b>Capital and Surplus, December 31, 2002 - Per Examination</b>					<b><u>\$ 27,129,024</u></b>

## **NOTES TO FINANCIAL STATEMENTS**

The Company has no special consents, permitted practices or orders from the state of Washington.

- A1            The Company's admitted deferred tax asset was overstated by \$4,046,257. This was corrected on the 2003 Annual Statement.
- A2            The Company reduced its Interest Maintenance Reserve (IMR) for an \$814,123 realized capital loss. The amount should have been reported as a realized loss in the Summary of Operations and included net of taxes as a component of the Asset Valuation Reserve (AVR) change. The IMR and AVR were appropriately adjusted, net of amortization and unrelated, normal activity.

### **ACKNOWLEDGEMENT**

The cooperation and assistance of the officers and employees of the Company during the examination are hereby acknowledged.

In addition to the undersigned, Susan Campbell, CPA, FLMI; Adrienne DeBella, Keith Henderson, CPA, CFE; Alexis S. Santos, FSA, MAAA; Michael V. Jordan, CPA, CFE, MHP and John Jacobson, AFE, all from the Washington State Office of the Insurance Commissioner participated in the examination and the preparation of this report.

Respectfully submitted,


A handwritten signature in black ink, appearing to read "John Gaynard", is written over a horizontal line.

John Gaynard, CFE, CPA, FLMI  
Examiner in Charge  
State of Washington

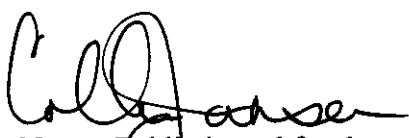
**AFFIDAVIT**

State of Washington       )  
                                      ) ss  
County of King             )

John Gaynard, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

  
\_\_\_\_\_  
John Gaynard, CPA, CFE, FLMI  
Examiner in Charge  
State of Washington

Subscribed and sworn to before me on this 4<sup>th</sup> day of March,  
2005.

  
\_\_\_\_\_  
Notary Public in and for the  
State of Washington

